HOUSING MARKET INFORMATION

HOUSING MARKET OUTLOOK
Sherbrooke CMA

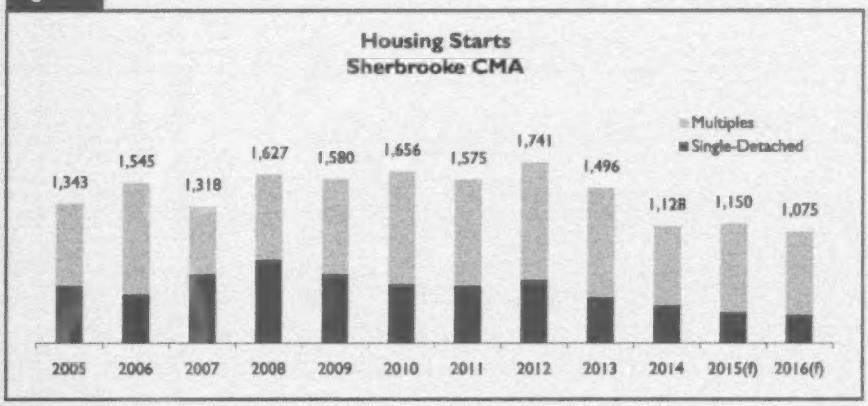
CANADA MORTGAGE AND HOUSING CORPORATION

Date Released: Spring 2015

Highlights

- Housing starts will increase slightly in 2015, to 1,150 units, and then weaken in 2016.
- Even though Centris® sales will pick up in 2015 (+4.5 per cent), the resale market will remain favourable to buyers.
- The average price of existing homes will remain at $223,000 this year and rise slightly next year.
- The rental housing vacancy rate will stay high in 2015 and 2016 (5.6 per cent).

Figure 1



Source: CMHC f: CMHC forecasts

The outlook is subject to uncertainty. Although point forecasts are presented in this publication, CMHC also presents risks where appropriate. The forecasts and historical data included in this document reflect information available as of April 20, 2015.

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HOME TO CANADIANS

New home market: activity will improve in 2015 and then decrease in 2016

In the Sherbrooke census metropolitan area (CMA), residential construction will be slightly stronger in 2015. Housing starts will post a small increase (+2 per cent), to 1,150 units, after experiencing a particularly difficult year in 2014 (-25 per cent). The housing starts results in 2015 will differ depending on the unit type. Single-detached home starts will decrease, while multi-unit housing starts will rise slightly, contrary to what was observed in 2014. In 2016, the new home market will resume its downward course, with total housing starts expected to decrease to 1,075 units (-6.5 per cent).

Foundations should be laid for 300 single-detached homes this year, or 69 fewer than last year. The pace of construction in this segment will continue to slow down in 2016, to some 250 units. Several factors will limit demand for new housing. First, potential buyers have lots of choice, as the supply of single-detached homes on the resale market reached a high in 2014. Also, the price difference between new and existing single-detached homes is increasingly widening, to the detriment of new homes. In this regard, a bylaw amendment adopted in 2014 by the City of Sherbrooke may be putting upward pressure on new home prices as a result of the change affecting land costs.[1] In fact, single-family new homes were sold at higher-than-typical prices in the first quarter of 2015. Finally, the aging of the population and the changes in household composition are making single-detached homes less attractive.

After slowing down significantly in 2014 (-28 per cent), multi-unit (semi-detached, row, condominium and apartment) housing starts should increase in 2015, to around 850 units, especially given the surge in condominium apartment construction. In 2016, activity in this segment will remain relatively stable (with some 800 housing starts). Ultimately, there will be three times more multi-unit housing starts than single-detached home starts in 2016. Increased international migration and the aging of the population are factors that will stimulate demand for multi-unit housing, to the detriment of single-detached homes.

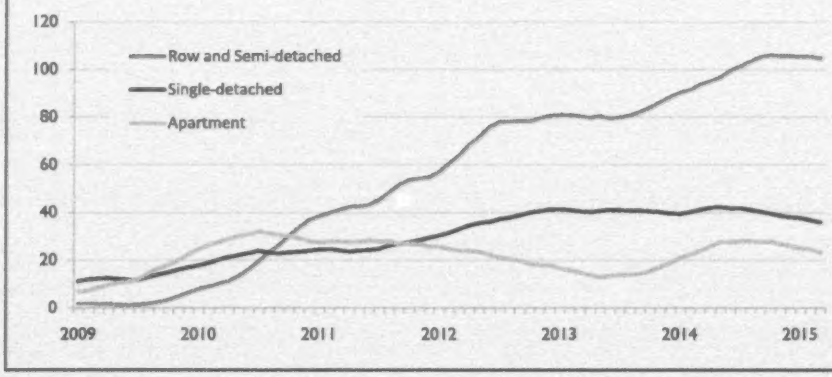
Semi-detached and row home construction will remain near the level recorded last year, at 250 units. Activity is not expected to pick up for such homes, as the inventory remains so high that some builders are even offering future buyers a rent-to-own option. In fact, the inventory is at an all-time high of some 110 semi-detached and row homes (see figure 2). Still, their affordability compared to single-detached houses and their smaller inventory on the existing home market will support demand for such homes.

In the apartment segment, a greater number of condominium units are expected to be started this year, given the interest shown by some developers. Potential buyers of condominiums still have a wide choice on the resale market. Therefore, condominium construction should be expected to decrease in 2016.

The pace of rental apartment construction will stay at around 400 units in 2015 and 2016. Activity will be supported by stronger demand for newer units,

Figure 2

Ownership Dwellings, Completed & Not-Absorbed Sherbrooke CMA*



Source: CMHC

*Smoothed data using a twelve-month moving average.

[1] Developers must now cover all the costs related to the installation of a water retention pond, costs that were previously assumed by the City of Sherbrooke.

if the low vacancy rate in this category (less than 3 per cent) is any indication, and by the addition of units on the retirement home market.

To conclude, it should be recalled that the need for new units will be essentially lower than before in the CMA. As was mentioned in previous reports, net household formation will be more moderate,[2] at about 1,100 households, in both 2015 and 2016.

Existing home market: transactions pick up after three years of decrease

For the third consecutive year, the number of Centris® transactions decreased in 2014 (-1.0 per cent). Still, activity began to pick up over the summer of 2014 and should continue to do so in 2015 and 2016.

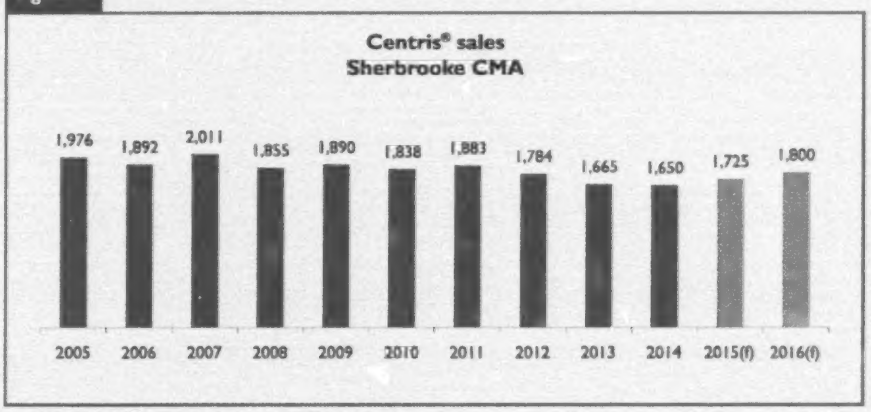
This increase in demand was essentially the result of significant employment gains made throughout 2014 and even in the first quarter of 2015. The recent decrease in mortgage rates will also support this demand. A greater number of buyers should therefore be expected on the resale market in 2015, which will result in a higher number of transactions.

In concrete terms, transactions should climb by 4.5 per cent in 2015 and surpass the 1,700-unit threshold (see figure 3). The gain should be similar in 2016, with transactions expected to increase by 4.3 per cent, to 1,800 units. Also, the anticipated rise in demand will not be sufficient to significantly reduce the number of homes for sale on the market, with new listings constantly being added. New listings increased in 2014 but should decrease in 2015. In fact, they dropped by 5 per cent in the first quarter of 2015, compared to the first quarter of 2014.

After reaching a high in 2014, existing homes for sale will decrease slightly in 2015 and 2016 but will stay above the levels of 2012 and 2013. Consequently, the market will remain favourable to buyers, despite conditions that will begin to tighten somewhat during the year (see figure 4).

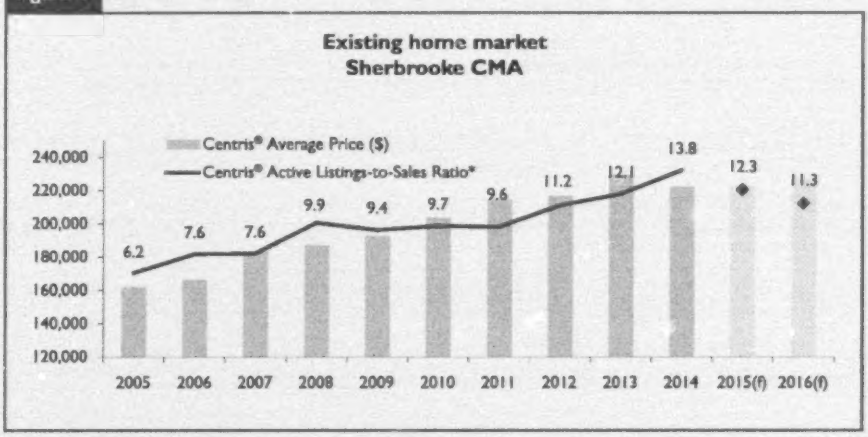
This situation is expected to have an impact on the growth in the average price, which, as a result of the anticipated pickup in activity, will start to rise again in 2015, after decreasing in 2014. Concretely, the average price will climb slightly in 2015 and 2016 and reach $227,000. It will therefore

Figure 3



Source: QFREB by Centris® f: CMHC forecasts

Figure 4



Source: QFREB by Centris® f: CMHC forecasts

* The market is generally considered to be balanced when this ratio is between 8 and 10.

[2] At the beginning of September 2014, the Institut de la statistique du Québec published an update of its demographic outlook (see Perspectives démographiques du Québec et des régions, 2011-2061).

increase by an average of 1 per cent each year, a rate well below the pace of the last 10 years (4.7 per cent on average).

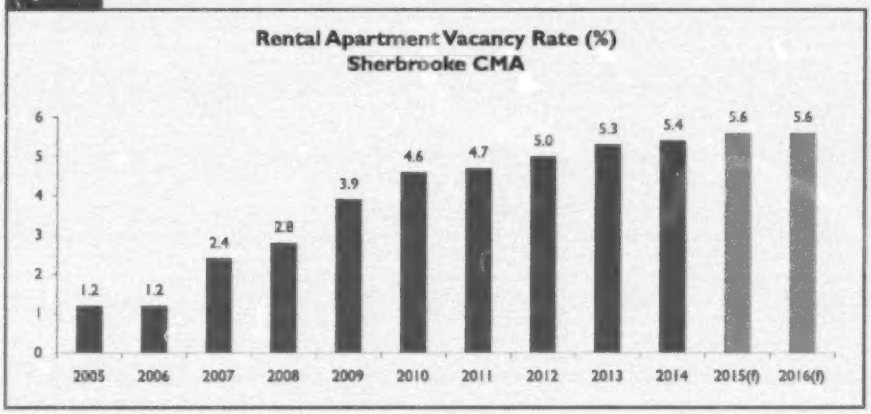
Rental market: no decrease in the vacancy rate on the horizon

Given the relatively favourable mortgage rates, many renters became homeowners in recent years. That environment, combined with the steady construction of rental dwellings, put upward pressure on the rental housing vacancy rate. In 2014, the average vacancy rate in the Sherbrooke area reached 5.4 per cent, the highest level in recent years. At the same time, the vacancy rate for newer rental buildings, built since 2000, was below 3 per cent, demonstrating strong demand for units in this category. This stimulated rental apartment starts, as evidenced by the start of construction on several large projects in the last year and a half. Another factor stimulating rental apartment construction is the low mortgage rates, as investors can get a good return on their equity.

In 2015 and 2016, the vacancy rate for the overall market will remain high, at 5.6 per cent (see figure 5). This rate will be stable compared to 2014, from a statistical standpoint, as supply and demand on the rental market will post similar increases.

Rental housing demand, for its part, will be stimulated by economic conditions and immigration policies that will encourage people to come and settle in the area. However, these positive effects will be partially offset by a stronger movement to homeownership that could even be amplified by the possibility for potential buyers to take advantage of a rent-to-own option, which is increasingly being offered in the area. As for supply, the growth in the rental housing stock will be fuelled by the large number of units that will be completed in 2015 and 2016.

Figure 5



Source: CMHC Rental Market Survey (October) f: CMHC forecasts

All in all, the forces of demand and supply will cancel each other, which will result in relatively stable market conditions. In addition, the arrival of new units on the market will also put upward pressure on the average rent.

Economic trends: conditions will continue to stimulate employment and migration

After several sluggish years, the Sherbrooke area recorded a net gain of 4,650 jobs in 2014. This was a significant result for future housing demand, especially given that most of the net gain was attributable to an increase in full-time jobs among people aged from 25 to 44.

However, it would be surprising for the results achieved in 2014 to recur in 2015, as consecutive years of strong growth are rare. Employment growth should in fact be expected to slow down to about 1 per cent in each of the next two years. Even with a favourable economic outlook for the area and the province, the expansion of the labour supply will be weaker, after having been strong in 2014 (+5 per cent). For this reason, coupled with the expected jobs gains, the unemployment rate is forecast to drop considerably in 2015 and 2016.

Given the weak Canadian dollar and accelerating economic growth in the United States, economic conditions are expected to continue to stimulate employment growth in the area, even though significant gains were registered in 2014. Another positive impact on employment in 2015 and 2016 is the increase in capital investments (machinery and equipment) in 2014 in, a sign that the area's companies are more confident. These investments should result in productivity gains followed by employment gains.

In 2014, exporting companies, especially in the manufacturing sector and the tourism industry, benefitted from the depreciation of the Canadian dollar against the U.S. dollar, as evidenced by employment gains in these sectors (see text box on page 7). For 2015 and 2016, the manufacturing sector and the tourism industry are expected to continue posting some strength. On the one hand, Tourism Eastern Townships began this past March an advertising campaign south of the border to attract between 25,000 and 30,000 additional American tourists in the area this summer. On the other hand, oil prices (and therefore the Canadian dollar) should not increase markedly in the medium term.

In regard to migration, better economic conditions in the area should attract and retain more people in 2015 and 2016. On the one hand, energy-producing Canadian provinces are no longer as much of an important hub for young Quebec workers and, on the other hand, efforts were made to increase immigrant retention in the area. It should be noted that, while international migration contributes to net migration in a greater proportion than before, only one immigrant out of every five still lives in the area five years after arriving[3], a low retention rate compared to the other areas of the province.

In summary, better economic conditions in the area had positive effects on employment last year. This will continue in 2015 and 2016 as we do not expect any significant change in the economic environment. This situation will also be favourable to gains in net migration. Consequently, positive impacts on housing demand are expected.

Mortgage rates are expected to remain at or close to current levels over the forecast horizon

Mortgage rates will continue to be supportive of housing demand. Consistent with the view of Canadian economic forecasters, CMHC expects interest rates to remain at or very close to current levels over the forecast horizon.

According to CMHC's base case scenario for 2015, the one-year mortgage rate is expected to be in the 2.30 to 3.50 per cent range, while the five-year rate is forecast to be within the 4.00 to 5.50 per cent range. For 2016, the one-year mortgage rate is expected to be in the 2.40 to 4.00 per cent range, while the five-year rate is forecast to be within the 4.20 to 6.20 per cent range.

[3] According to a recent study by a Sherbrooke organization, Actions interculturelles de développement et d'éducation (AIDE), from 2006 to 2010, 5,667 immigrants settled in the Eastern Townships. In 2011, more than 4,400 of them had left the area.

Trends at a glance

Key Factors and their Effects on Housing Starts	
Mortgage Rates	Mortgage rates will remain low by historical standards and supportive of housing demand.
Employment	Employment rebounded in 2014 and will continue to grow in 2015 and 2016, but at a moderate pace, as a result, in part, of the impact of population aging on the available labour force. These gains will promote a pickup in housing demand.
Income	The rise in average weekly earnings in 2014 and at the beginning of 2015 was slightly above the inflation rate. The acceleration in real income growth could stimulate housing demand.
Population	The composition of net migration and the aging of the population will further promote the demand for apartments and rental units. In the medium term, housing starts will be limited by lower net household formation.
Resale Market	Conditions on the resale market will remain favorable to buyers in 2015 and 2016, which will limit both price growth and demand for new housing.

Forecast risks

In addition to factors with impacts at the national and provincial levels, there are some risk factors specific to the Sherbrooke area, such as the following:

- Economic growth could be weaker than expected and not have the desired effect on job creation. If this were the case, housing demand would be weaker. It would therefore be more difficult to reduce the inventory of new and existing homes to be absorbed.
- The impact of the change made to municipal regulations on the cost of lots could be more significant. The subsequent effect on residential development could therefore be more important than expected.
- Despite the soft conditions on the condominium resale market, the growing interest among builders for condominiums could have an upward impact on our outlook.

Spotlight on...

Widespread employment gains among the sectors in 2014

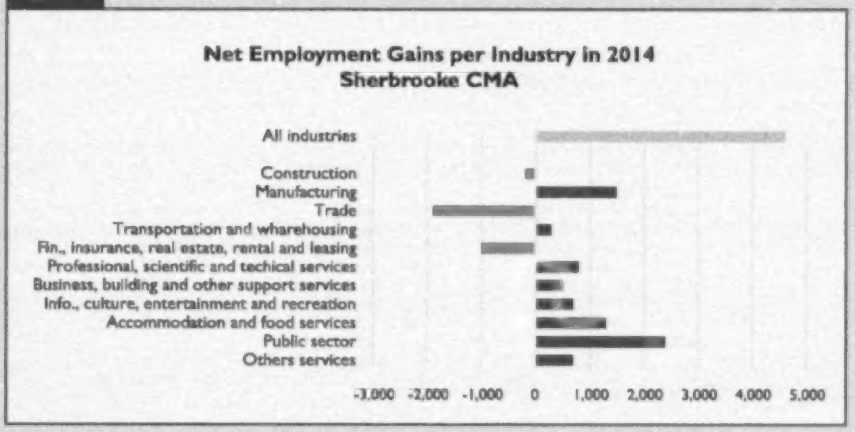
In light of employment data, the Sherbrooke CMA benefitted from favourable economic conditions in 2014. Almost all of the area's sectors (80 per cent) recorded a net increase in staff. Also, the analysis of results by sectors revealed that the weak Canadian dollar was favourable to the manufacturing, accommodation and food services sectors. According to the data published by Statistics Canada, companies in these sectors and the public sector hired the most people in 2014. Also, the manufacturing and public sectors offer higher than average compensation, which helps stimulate housing demand.

It would seem that job losses in the construction, finance, insurance and real estate sectors were the result of a slower housing market in the area in recent years. The contraction in the trade sector is rather part of a structural change. This sector, even at the national level, is facing its share of challenges, including those resulting from the boom of e-commerce.

Over the next few years, net job creation should remain positive in the manufacturing, transportation, warehousing, accommodation and food services sectors. As previously mentioned the loonie should remain below parity with the greenback in the medium term, such that these sectors will be able to keep the gains made in terms of competitiveness with their American counterparts.

To conclude, it would be surprising for the public sector to stand out as much as it did in the next few years, given the current budget cuts by the provincial government.

Figure 6



Source: Statistics Canada
*Education, health and public administration.

Forecast Summary
Sherbrooke CMA
Spring 2015

	2012	2013	2014	2015(F)	% chg	2016(F)	% chg
New Home Market							
Starts:							
Single-Detached	610	442	369	300	-18.7	275	-8.3
Multiples	1,131	1,054	759	850	12.0	800	-5.9
Starts - Total	1,741	1,496	1,128	1,150	2.0	1,075	-6.5
Average Price ($)							
Single-Detached	279,010	303,165	308,513	325,000	5.3	330,000	1.5
Median Price ($):							
Single-Detached	260,000	292,500	290,000	310,000	6.9	315,000	1.6
New Housing Price Index (% chg) (Que.)	1.7	1.0	0.3	n/a	-	n/a	-
Resale Market							
Centris® Sales	1,784	1,665	1,650	1,725	4.5	1,800	4.3
Centris® New Listings	3,630	3,578	3,338	3,500	4.9	3,400	-2.9
Centris® Active Listings	1,666	1,672	1,899	1,775	-6.5	1,650	-7.0
Centris® Average Price ($)	216,662	229,483	222,204	223,000	0.4	227,000	1.8
Rental Market							
October Vacancy Rate (%)	5.0	5.3	5.4	5.6	0.2	5.6	0.0
Two-bedroom Average Rent (October) ($)	578	591	604	620	2.6	635	2.4
Economic Overview							
Mortgage Rate (1 year) (%)	3.17	3.08	3.14	2.30 to 3.50	-	2.40 to 4.00	-
Mortgage Rate (5 year) (%)	5.27	5.24	4.88	4.00 to 5.50	-	4.20 to 6.20	-
Annual Employment Level	100,200	97,200	101,800	102,500	0.7	103,500	1.0
Employment Growth (%) - excluding Magog	-3.5	-3.0	4.7	0.7	-	1.0	-
Unemployment rate (%)	8.0	7.1	7.2	6.7	-	6.2	-
Net Migration	2,082	1,957	1,750	1,900	8.6	2,000	5.3

[1]The Centris® system contains all the listings of Québec real estate brokers.

[2]Source: CMHC (Starts and Completions Survey, Market Absorption Survey), adapted from Statistics Canada (CANSIM), Statistics Canada (CANSIM), Centris® Statistics. CMHC Forecast (2015-2016)

NOTE: Rental universe = Privately initiated rental apartment structures of three units and over

DEFINITIONS AND METHODOLOGY

New Home Market

Historical home starts numbers are collected through CMHC's monthly **Starts and Completions Survey**. Building permits are used to determine construction sites and visits confirm construction stages. A **start** is defined as the beginning of construction on a building, usually when the concrete has been poured for the whole of the structure's footing, or an equivalent stage where a basement will not be part of the structure.

Single-Detached Start:
The start of a building containing only one dwelling unit, which is completely separated on all sides from any other dwelling or structure.

Semi-Detached Start:
The start of each of the dwellings in a building containing two dwellings located side-by-side, adjoining no other structure and separated by a common or party wall extending from ground to roof.

Row (or Townhouse) Start:
Refers to the commencement of construction on a dwelling unit in a row of three or more attached dwellings separated by a common or party wall extending from ground to roof.

Apartment and other Starts:
Refers to the commencement of construction on all dwellings other than those described above, including structures commonly known as stacked townhouses, duplexes, triplexes, double duplexes and row duplexes.

Average and Median Single Detached Home Prices:
Are estimated using CMHC's **Market Absorption Survey**, which collects home prices at absorption and measures the rate at which units are sold or rented after they are completed. Dwellings are enumerated each month after a structure is completed until full absorption occurs. The term "**absorbed**" means that a housing unit is no longer on the market as it has been sold or rented.

New Home Price Indexes:
Changes in the New Home Price Indexes are estimated using annual averages of Statistics Canada's monthly values for New Housing Price Indexes (NHPI).

Resale Market

Historical resale market data in the summary tables of the Housing Market Outlook Reports refers to residential transactions through the Multiple Listings Services (MLS®) as reported by The Canadian Real Estate Association (CREA). In Quebec, this data is obtained by the Centris® listing system via the Quebec Federation of Real Estate Boards.

MLS® (Centris® in the province of Quebec) Sales:
Refers to the total number of sales made through the Multiple Listings Services in a particular year.

MLS® (Centris® in the province of Quebec) Average Price:
Refers to the average annual price of residential transactions through the Multiple Listings Services.

Rental Market

Rental Market vacancy rates and two bedroom rents information is from Canada Mortgage and Housing Corporation's (CMHC's) October Rental Market Survey (RMS). Conducted on a sample basis in all urban areas with populations of 10,000 and more, the RMS targets privately initiated structures with at least three rental units, which. have been on the market for at least three months. The survey obtains information from owners, managers, or building superintendents through a combination of telephone interviews and site visits.

Vacancy Rate:
The vacancy rate refers to the average vacancy rate of all apartment bedroom types. A unit is considered vacant if, at the time of the survey, it is physically unoccupied and available for immediate rental.

Two Bedroom Rent:
The rent refers to the average of the actual amount tenants pay for two bedroom apartment units. No adjustments are made for the inclusion or exclusion of amenities and services such as heat, hydro, parking, and hot water.

Economic Overview

Labour Force variables include the Annual Employment Level, Employment Growth, Unemployment Rate. Source: Statistics Canada's Labour Force Survey.

Net Migration:
Sum of net interprovincial (between provinces), net intra-provincial (within provinces), net international (immigration less emigration), returning Canadians and temporary (non-permanent) residents as provided to the CANSIM database by Statistics Canada's Demography Division. Sources of inter-provincial and intra-provincial migration data include a comparison of addresses from individual income tax returns for two consecutive years from Canada Revenue Agency (CRA) taxation records. The migration estimates are modelled, with the tax file results weighted to represent the whole population.

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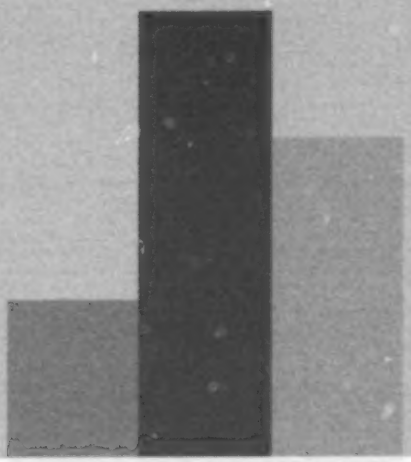

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